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**COMPARATIVE ANALYSIS ON THE PROFITABILITY  
DETERMINANTS OF MALAYSIAN ISLAMIC AND  
CONVENTIONAL BANKS**



**MASTER IN ISLAMIC FINANCE AND BANKING  
UNIVERSITY UTARA MALAYSIA  
JUNE 2018**

**COMPARATIVE ANALYSIS ON THE PROFITABILITY DETERMINANTS  
OF MALAYSIAN ISLAMIC AND CONVENTIONAL BANKS**



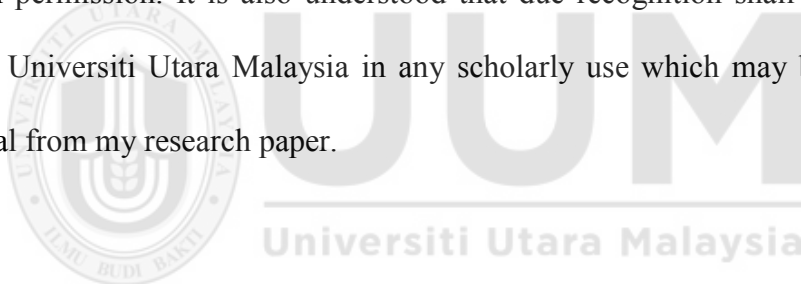
**By  
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**UUM**  
**Universiti Utara Malaysia**

**Research Paper Submitted to  
Othman Yeop Abdullah Graduate School of Business,  
Universiti Utara Malaysia,  
in Partial Fulfillment of Requirement for the Master in Islamic Finance and  
Banking**

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## ABSTRACT

Islamic Banking has become competitive against conventional banking since it is one of the fastest growing institutions nowadays. Therefore, it is reasonable to expect that the performance of both Islamic and conventional banks has become the center of attention particularly in term of their profitability. The main objective of this study is to compare the bank-specific factor that mainly impacts on the profitability of Islamic and Conventional banks. The dependent variable for this study is Return on Asset (ROA) while the independent variables are Capital Ratio (ETA), Bank Size (SIZE), Liquidity Ratio (LIQR) and Deposit Ratio (DTA). Secondary data was used from 16 Islamic banks (144 observations) and 22 Conventional banks in Malaysia (183 observations), over the 2008 - 2016 period. The study found that the bank-specific factors, namely ETA and DTA have a significant impact on the profitability of Islamic banks in Malaysia. Meanwhile, for the Conventional banks in Malaysia, SIZE, LIQR, and DTA are found to be significant to their profitability.

**Keywords:** profitability, Islamic banks, Conventional banks, bank-specific factors



## ABSTRAK

Perbankan Islam telah menjadi persaingan terhadap perbankan konvensional kerana ia merupakan salah satu institusi yang paling cepat berkembang pada masa kini. Oleh itu, adalah munasabah untuk menjangkakan prestasi kedua-dua jenis bank ini menjadi perhatian terutamanya dari aspek keuntungan mereka. Objektif utama kajian ini adalah untuk membandingkan faktor dalaman bank yang memberi kesan terutamanya kepada keuntungan bank Islam dan bank Konvensional. Pemboleh ubah bersandar untuk kajian ini adalah Pulangan Atas Aset (ROA) manakala pembolehubah tidak bersandar adalah Nisbah Modal (ETA), saiz bank (SIZE), Nisbah Kecairan (LIQR) dan Nisbah Deposit (DTA). Data sekunder digunakan dari 16 bank Islam (144 pemerhatian) dan 22 bank konvensional di Malaysia (183 pemerhatian), sepanjang tempoh 2008 - 2016. Kajian mendapati faktor-faktor khusus bank, iaitu ETA dan DTA mempunyai kesan yang signifikan ke atas keuntungan bank Islam di Malaysia. Sementara itu, bagi bank Konvensional di Malaysia, SIZE, LIQR dan DTA adalah penyumbang signifikan kepada keuntungan mereka.

**Kata kunci:** keuntungan, bank Islam, bank Konvensional, faktor dalaman bank



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## TABLE OF CONTENTS

<b>Page</b>		
TITLE		
DECLARATION		i
PERMISSION TO USE		ii
ABSTRACT		iii
ABSTRAK		iv
ACKNOWLEDGEMENT		v
TABLE OF CONTENT		vi
LIST OF APPENDICES		ix
LIST OF TABLES		x
LIST OF FIGURES		xi
LIST OF ABBREVIATIONS		xii
<b>CHAPTER 1</b>	<b>BACKGROUND OF THE STUDY</b>	
1.0	Introduction	1
1.1	Background of the study	1
1.2	Problem Statement	5
1.3	Research Question	8
1.4	Research Objective	8
1.5	Significance of the Study	8
1.6	Scope of Study	9
1.7	Organization of the Thesis	9
<b>CHAPTER 2</b>	<b>LITERATURE REVIEW</b>	
2.0	Introduction	11
2.1	Concept of Profitability	11
2.2	Bank-specific Factors	12
2.2.1	Capital	12
2.2.2	Bank size	14
2.2.3	Liquidity	15



3.2.4	Deposit	17
2.3	Related Theory	18
2.3.1	Structure Conduct Performance Theory	18
2.3.2	Signaling Theory	19
2.3.3	Financial Intermediation Theory	19
2.4	Summary	20

## **CHAPTER 3 METHODOLOGY**

3.0	Introduction	21
3.1	Research Framework	21
3.2	Hypotheses Development	22
3.3	Research Design	23
3.4	Operational Definition and Measurement	24
3.4.1	Dependent Variable	24
3.4.2	Independent Variable	24
3.4.2.1	Capital Adequacy (CAR)	24
3.4.2.2	Bank size	25
3.4.2.3	Liquidity	25
3.4.2.4	Deposit	25
3.5	Data Collection	26
3.5.1	Data Sources	26
3.5.2	Sample	26
3.5.3	Data Analysis	30
3.5.3.1	Descriptive Statistic	30
3.5.3.2	Correlation Analysis	30
3.5.3.3	Multiple Regression Analysis	30
3.5.3.4	Fixed Effect Model	31
3.5.3.5	Model Specification Multiple Regression Analysis	31
3.6	Summary	32

## **CHAPTER 4 RESULTS AND DISCUSSION**

4.0	Introduction	33
4.1	Descriptive Statistics of Variables	33
4.2	Correlation between Variables	37
4.3	Multiple Regression Analysis	39
	4.3.1 Bank-specific factors for Islamic banks in Malaysia	40
	4.3.2 Bank-specific factors for Conventional banks in Malaysia	43
4.4	The Summary of the Result of the Relationship between Bank-Specific Factors and Profitability of Islamic and Conventional Banks in Malaysia	44
4.6	Summary	47

## **CHAPTER 5 CONCLUSION AND RECOMMENDATION**

5.0	Introduction	48
5.1	Discussion on the result	48
	5.1.1 Relationship between Bank-specific Factors and Profitability in Islamic and Conventional banks in Malaysia	49
5.2	Recapitulation of the Findings	52
	5.2.1 Objective 1	52
	5.2.2 Objective 2	53
	5.2.3 Objective 3	54
5.3	Contribution of the Study	55
5.4	Limitation of the Study	55
5.5	Suggestion for Future Research	56

<b>REFERENCES</b>	57
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## LIST OF APPENDICES

		<b>Page</b>
APPENDIX I	Results of Descriptive Analysis	65
APPENDIX II	Result of the Multiple Regression for Islamic Banks in Malaysia	66
APPENDIX III	Result of the Multiple Regression for Conventional Banks in Malaysia	67



## LIST OF TABLES

	<b>Page</b>
Table 1.1	Differences between Islamic and Conventional banks 4
Table 3.1	Summary of Operational Definition and Measurement of Variables 26
Table 3.2	List of Islamic banks in Malaysia 28
Table 3.3	List of Conventional banks in Malaysia 29
Table 4.1	Descriptive Statistics of Variables for Islamic Banks in Malaysia 34
Table 4.2	Descriptive Statistics of Variables for Conventional Banks in Malaysia 35
Table 4.3	Descriptive Statistics of Variables for Islamic and Conventional Banks in Malaysia 36
Table 4.4	Correlation Matrix for Islamic banks in Malaysia 38
Table 4.5	Correlation Matrix for Conventional banks in Malaysia 38
Table 4.6	Bank-specific Factors on Return of Asset (ROA) of Islamic Banks in Malaysia 39
Table 4.7	Bank-specific Factors on Return of Asset (ROA) of Conventional Banks in Malaysia 42
Table 4.8	Summary of the Multiple Regression Result of Bank-Specific Factors on Profitability of Islamic Banks in Malaysia 45
Table 4.9	Summary of the Multiple Regression Result of Bank-Specific Factors on Profitability of Conventional Banks in Malaysia 46
Table 5.1	Summary Result of Bank-Specific Factors Impact on Islamic and Conventional Banks Profitability 49

## LIST OF FIGURES

		<b>Page</b>
Figure 1.1	Profitability (ROAA) for Islamic and Conventional banks in Malaysia	6
Figure 3.1	Theoretical Framework	21



## LIST OF ABBREVIATIONS

BIMB	Bank Islam Malaysia Berhad
BNM	Bank Negara Malaysia
ETA	Capital Ratio
DTA	Deposit Ratio
FEM	Fixed Effects Model
IBS	Islamic Banking Scheme
LIQR	Liquidity Ratio
PWSBH	Perbadanan Wang Simpanan Bakal-Bakal Haji
ROA	Return on Asset
ROAA	Return on Average Asset
ROE	Return on Equity
SCP	Structure Conduct Performance
SIZE	Bank Size

# **CHAPTER ONE**

## **INTRODUCTION**

### **1.0 Introduction**

This research aimed to study the impact of bank-specific factors upon the profitability of Islamic and Conventional banks in Malaysia. This chapter mainly discusses the outline and overall context of the study. In particular, it consists of a background of the study as a general discussion of the topic, research problem as a discussion on the arising issue, research questions and research objectives as a guideline to this topic. On the other hand, there is the significance of the study, scope and limitation of study and organization of study were included in this chapter.

### **1.1 Background of the study**

Banking industry plays an undisputed role in the development of the economic growth (Chapra, 2008) as it ensures the financial resources flows efficiently from the depositors to the borrowers. At the present time, the banking system in Malaysia consists of investment banks, commercial banks, international Islamic banks and Islamic banks which are the main money resources as well as the key supply of financing in order to strengthen the Malaysian economic activities (Omar et al. (2017).

Malaysia has a unique banking system where Islamic and Conventional banks operate side by side and it has appeared as the first country to implement a dual banking system. Islamic banking system was introduced in Malaysia in 1963 with the establishment of Perbadanan Wang Simpanan Bakal-Bakal Haji (PWSBH). PWSBH

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## APPENDICES

### APPENDIX I

#### Results of Descriptive Analysis for Islamic Banks in Malaysia

Date: 04/18/18 Time: 01:20 Sample: 2008 2016					
	ROA	CAR	SIZE	LIQUIDITY	DEPOSIT
Mean	0.021294	0.086651	7.171519	0.595964	0.007974
Median	0.020565	0.074505	7.153967	0.639455	1.42E-05
Maximum	0.048185	0.351509	8.259581	0.832519	0.077652
Minimum	-0.043267	0.031872	6.261174	0.000804	0.000000
Std. Dev.	0.009596	0.044136	0.414222	0.142406	0.014446
Skewness	-1.835365	2.434990	0.111666	-1.548530	2.380556
Kurtosis	16.22142	11.57536	2.726201	6.291608	9.119031
Jarque-Bera	1129.681	583.5205	0.749060	122.5588	360.6644
Probability	0.000000	0.000000	0.687612	0.000000	0.000000
Sum	3.066341	12.47781	1032.699	85.81880	1.148186
Sum Sq. Dev.	0.013167	0.278563	24.53591	2.899970	0.029842
Observations	144	144	144	144	144

#### Results of Descriptive Analysis for Conventional Banks

Date: 04/18/18 Time: 01:17 Sample: 2008 2016					
	ROA	CAR	SIZE	LIQUIDITY	DEPOSIT
Mean	0.031236	0.182397	7.372085	0.890081	0.050000
Median	0.027644	0.097051	7.602822	0.577427	0.021244
Maximum	0.194632	0.994644	8.695536	9.550673	0.723107
Minimum	0.000000	0.051638	4.346685	0.000000	0.000000
Std. Dev.	0.020799	0.220318	0.801457	1.783036	0.105100
Skewness	5.098322	2.614917	-0.663900	4.110348	3.846259
Kurtosis	35.27256	8.594211	3.117785	18.26984	18.77287
Jarque-Bera	8734.357	447.1785	13.54904	2293.202	2348.181
Probability	0.000000	0.000000	0.001143	0.000000	0.000000
Sum	5.716156	33.37865	1349.092	162.8849	9.149976
Sum Sq. Dev.	0.078736	8.834255	116.9047	578.6175	2.010392
Observations	183	183	183	183	183



## APPENDIX II

### Result of the Multiple Regression for Islamic Banks in Malaysia

Dependent Variable: ROA				
Method: Panel EGLS (Cross-section weights)				
Date: 04/07/18 Time: 01:56				
Sample: 2008 2016				
Periods included: 9				
Cross-sections included: 16				
Total panel (balanced) observations: 144				
Linear estimation after one-step weighting matrix				
White cross-section standard errors & covariance (d.f. corrected)				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.019302	0.026135	0.738537	0.4616
CAR	0.057759	0.018436	3.132978	0.0022
DEPOSIT	-0.077523	0.026311	-2.946394	0.0038
LIQUIDITY	0.001323	0.002077	0.636968	0.5253
SIZE	-0.000444	0.003858	-0.115038	0.9086
Effects Specification				
Cross-section fixed (dummy variables)				
Weighted Statistics				
R-squared	0.606240	Mean dependent var	0.036515	
Adjusted R-squared	0.545906	S.D. dependent var	0.022153	
S.E. of regression	0.007422	Sum squared resid	0.006830	
F-statistic	10.04804	Durbin-Watson stat	1.539090	
Prob(F-statistic)	0.000000			
Unweighted Statistics				
R-squared	0.378580	Mean dependent var	0.021294	
Sum squared resid	0.008182	Durbin-Watson stat	1.588352	

## APPENDIX III

### Result of the Multiple Regression for Conventional Banks in Malaysia

Dependent Variable: ROA				
Method: Panel EGLS (Cross-section weights)				
Date: 04/05/18 Time: 11:53				
Sample: 2008 2016				
Periods included: 9				
Cross-sections included: 22				
Total panel (unbalanced) observations: 183				
Linear estimation after one-step weighting matrix				
White cross-section standard errors & covariance (d.f. corrected)				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.120308	0.011524	10.43999	0.0000
CAR	-0.007034	0.007548	-0.931823	0.3529
DEPOSIT	-0.015696	0.006411	-2.448245	0.0155
LIQUIDITY	0.010427	0.003617	2.882437	0.0045
SIZE	-0.013061	0.001728	-7.558320	0.0000
Effects Specification				
Cross-section fixed (dummy variables)				
Weighted Statistics				
R-squared	0.882523	Mean dependent var	0.129523	
Adjusted R-squared	0.863817	S.D. dependent var	0.087623	
S.E. of regression	0.013588	Sum squared resid	0.028988	
F-statistic	47.17731	Durbin-Watson stat	1.393300	
Prob(F-statistic)	0.000000			
Unweighted Statistics				
R-squared	0.496210	Mean dependent var	0.031236	
Sum squared resid	0.039667	Durbin-Watson stat	3.533612	